МІНІСТЕРСТВО ОСВІТИ І НАУКИ,
МОЛОДІ ТА СПОРТУ УКРАЇНИ
ХАРКІВСЬКА НАЦІОНАЛЬНА АКАДЕМІЯ
МІСЬКОГО ГОСПОДАРСТВА

МЕТОДИЧНІ ВКАЗІВКИ
ДЛЯ ОРГАНІЗАЦІЇ ПРАКТИЧНОЇ РОБОТИ

З ДИСЦИПЛІНИ «ІНОЗЕМНА МОВА» (АНГЛІЙСЬКА МОВА)

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Методичні вказівки для організації практичної роботи студентів економічних спеціальностей у першому та другому триместрах згідно з затвердженою робочою програмою навчальної дисципліни «Іноземна мова», укладеної відповідно освітньо-кваліфікаційним вимогам до знань і вмінь студентів напрямів підготовки 6.030504 «Економіка підприємства», 6.030509 – «Облік і аудит», які в майбутньому будуть працювати у сфері економіки підприємства та обліку і аудиту.

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INTRODUCTION

These educational materials are designed for the ESP students of economics of the 1st year of studies to develop their knowledge and skills in English language.

This manual is based on the authentic texts from different sources concerning cross-cultural issues. It contains the tasks for reading and translation, vocabulary tasks and tasks for self-study.
Each unit contains:

- an authentic text for reading and translation;
- comprehension exercises;
- key vocabulary according to the topic. All key words are taken from the basic text;
- exercises for memorization and mastering key vocabulary;
- supplementary reading
- supplementary exercises

The manual is recommended for practical lessons

UNIT 1. ECONOMICS AS A SCIENCE. THE FIRST MODERN ECONOMISTS.

Task 1. Read the text and answer the questions.

Key words: economics, science, trade, exchange, to acquire, discipline, industry, commerce, definition

WHAT IS ECONOMICS?

Economy is as old as hills. It is probably the first art which man acquires. When in ancient time some people went out to hunt while others stayed to defend the fire and still other traded (exchange) some things for other ones, in all these cases we had economy.

But Economics as an academic discipline is new. The first important book on Economics was published in 1776. It was “The Wealth of Nations” written by Adam Smith (1723-1790). The author of this book was a Scottish economist. When he published the book Adam Smith was 53 years old. In the book he described the new world of industry and commerce. The fact is that his book founded classical economics modern for that time.

Since that time the subject developed rapidly. Now there are many branches of the subject. They are microeconomics, international economics, econometrics and so on.

There is an economic aspect to almost any topic we mention – education, health care, religion, employment, housing, transport, defence, etc.

Economics is a theory of how society works. It seems to be clear. However, it is difficult to define economics. There are many definitions.

The great classical economist Alfred Marshall defined: “Economics is the study of man in the everyday business of life”. J. Beardshaw, a British economist, gave more modern definition. It is: “The human science which studies the relationship between resources and the various users which compete for these resources”.

1. What is the first book on Economics?
2. What are the branches of this subject?
3. Where do we use economics?
4. What are the main definitions of economics?

Task 2. Choose an appropriate word from the box to complete the following sentences.

Resources production economic ancient economics economists market

1) In ________times in primitive societies there was no private property.

2) __________is a science that analyzes what, how, and for whom society produces.

3) In industrial Western countries markets are to allocate __________.

4) A free _______economy has no government intervention.

5) The ideas of Adam Smith, the famous Scottish economist, have been studied by _________for over two hundred years.

6) _________are to regulate or plan ___________and consumption.

7) __________statistics are of interest to economic policy decision-makers.

Task 3. Read the sentences and say if they are true or false.

1) Economy is as old as hills. T/F

2) But Economics as an academic discipline is not new. T/F

3) The first important book on Economics was published in 1876. T/F

4) The author of "The Wealth of Nations" was a Scottish philosopher. T/F

5) Economics is a theory of how society works. T/F

6) The great classical economist Alfred Marshall defined: "Economics is the study of man in the everyday business of life". T/F

Task 4. Scan the following reading for the answers to the questions below:

1. What two groups are discussed?
2. How were they different from each other?
3. What is "favorable balance of trade"?
4. What is "laissez faire" and with which group is the term associated?

The First Modern Economists

The Mercantilists. Between the 16th and 18th centuries, the major countries of Europe believed in the economic theory of mercantilism. Mercantilists argued that nations should behave as if they were merchants competing with one another for profit. Accordingly, governments should support industry by enacting laws designed to keep labor and other production costs low, and exports high. In this way the nation should achieve what was called a "favorable balance of trade".

"Favorable balance of trade" described a situation in which export exceeded imports. The excess, which was like profits to a merchant, would result in an increase in the nation's supply of gold and silver. And, as most people agreed in those days, the true measure of a nation's wealth was its hoard of gold and silver.

To achieve favorable trade balances, the major European powers sought to acquire colonies. Colonies, it was thought, could provide the "mother country" with cheap labour, raw materials and a market for its manufactured goods.

In an effort to attain these goals in their American colonies, the British, for example, enacted the Navigation Acts. The Navigation Acts protected British industry by prohibiting the colonies from producing certain goods like hats, woolen products and wrought iron. The laws also listed certain "enumerated articles" (mostly raw materials) which could not be sold to buyers in countries other than England.

Resentment towards the Navigation Acts was so great that they are regarded as one of the principal causes of the Revolutionary War.

Today there are people who still argue that their country should promote a "favorable balance of trade", that their national government should do what it can to restrict imports and promote exports. For this reason, they are often described as neo-mercantilists or “new” mercantilists.

The Physiocrats. For one group of 18th –century French philosophers and economists, the suggestion that nations should go out of their way to protect business and industry made no sense at all. These were the physiocrats.

The physiocrats argued that the products of agriculture and other natural resources were the true source of wealth. Since these were God-given, it made little sense for government to go out of its way to help business and industry increase profits. For similar reasons, they opposed government efforts to promote a “favorable balance of trade”.

In other words, since real wealth came from the land, it followed that the wisest thing government could do would be to keep its hands off business and let nature take its course. This idea was expressed in the slogan “laissez faire” (let people do as they choose).

Interestingly, the 200-year-old argument between those favoring regulation of the economy and those supporting “laissez faire” is still with us. Whether the problem involves the individuals (like those living in the poverty and unemployment) or institutions (such as a rising tide of business or bank failures), there are those who find the solution in government intervention, and others who favor “laissez faire”, letting natural economic forces take their course.

Questions for understanding

Working with a partner do the following tasks. Share your ideas with the whole class.

1. Write a definition for each of the two groups of economists discussed in the article.
2. Identify the neo-mercantilists.
3. Can you name any individuals or groups of people in your country or abroad who could be described as neo-mercantilists?
4. In the United States today, opinion about economic policy continues to be divided into two schools of thought similar to those described in the article. Is this true in your country? Provide examples to support your opinion.

UNIT 2. MICROECONOMICS AND MACROECONOMICS

Task 1. Read and translate the text

Key words: to allocate, limited resources, to determine, market failure, elasticity of products, competition, aggregate trends

Microeconomics and Macroeconomics

Microeconomics is a branch of economics that studies how individuals, households, and firms make decisions to allocate limited resources, typically in markets where goods or services are being bought and sold.

Microeconomics examines how these decisions and behaviors affect the supply and demand for goods and services, which determines prices, and how prices, in turn, determine the supply and demand of goods and services.

Macroeconomics, on the other hand, involves the "sum total of economic activity, dealing with the issues of growth, inflation, and unemployment and with national economic policies relating to these issues" and the effects of government actions (e.g., changing taxation levels) on them.

One of the goals of microeconomics is to analyze market mechanisms that establish relative prices amongst goods and services and allocation of limited resources amongst many alternative uses. Microeconomics analyzes market failure, where markets fail to produce efficient results, as well as describing the theoretical conditions needed for perfect competition. Significant fields of study in microeconomics include markets under asymmetric information, choice under uncertainty and economic applications of game theory. Also considered is the elasticity of products within the market system.

Macroeconomics is a branch of economics that deals with the performance, structure, and behavior of the economy as a whole. Macroeconomists study and seek to understand the determinants of aggregate trends in the economy with particular focus on national income, unemployment, inflation, investment, and international trade. In contrast, microeconomics is primarily focused on the determination of prices and the role of prices in allocating scarce resources.

While macroeconomics is a broad field of study, there are two areas of research that are emblematic of the discipline: the attempt to understand the causes and consequences of short-run fluctuations in national income (the business cycle), and the attempt to understand the determinants of long-run economic growth (increases in national income).

Macroeconomic models and their forecasts are used by both governments and large corporations to assist in the development and evaluation of economic policy and business strategy.

Task 2. Answer the following questions:

1. What is microeconomics?
2. What does microeconomics examine?
3. What is the main goal of microeconomics?
4. What fields does microeconomics analyze?
5. What is macroeconomics?
6. What does macroeconomics study?
7. Characterize the areas of research of macroeconomics.
8. Whom are macroeconomics models are used by?

Task 3. Fill in the gaps using the word from the box

political economy financial economics health economics public finance urban economics labor economics economic history

Applied microeconomics

Applied microeconomics includes a range of specialized areas of study, many of which draw on methods from other fields. Industrial organization and regulation examines topics such as the entry and exit of firms, innovation, role of trademarks. Law and economics applies microeconomic principles to the selection and enforcement of competing legal regimes and their relative efficiencies.________ ________ examines wages, employment, and labor market dynamics.______ _________ (also called public economics) examines the design of government tax and expenditure policies and economic effects of these policies (e.g., social insurance programs).________ _______ examines the role of political institutions in determining policy outcomes._______ ________ examines the organization of health care systems, including the role of the health care workforce and health insurance programs.,________ ________ which examines the challenges faced by cities, such as are sprawl, air and water pollution, traffic congestion, and poverty, draws on the fields of urban geography and sociology. The field of _______ _______ examines topics such as the structure of optimal portfolios, the rate of return to capital, econometric analysis of security returns, and corporate financial behavior. The field of________ examines the evolution of the economy and economic institutions, using methods and techniques from the fields of economics, history, geography, sociology, psychology, and political science.

UNIT 3. ECONOMIC SYSTEMS.

Task 1. Read and translate the text.

Key words: economics, economic, economical, command economy, free market economy, mixed economy, society, demand, good, service, market, to allocate, consumption, decision, intervention, government intervention, level, restriction, the former, the latter, government regulation, importance.

Market and Command Economies

Economics is a science that analyzes what, how, and for whom society produces. The central economic problem is to reconcile the conflict between people's unlimited demands with society's ability to produce goods and services.

In industrial Western countries markets are to allocate resources. The market is the process by which production and consumption are coordinated through prices.

In a command economy, a central planning office makes decisions on what, how and for whom to produce. Economy cannot rely entirely on command, but there was extensive planning in many Soviet block countries.

A free market economy has no government intervention. Resources are allocated entirely through markets.

Modern economies in the West are mixed and rely mainly on the market but with a large dose of government intervention. The optimal level of government intervention remains a problem which is of interest to economists.

The degree of government restrictions differs greatly between countries that have command economies and countries that have free market economies. In the former, resources are allocated by central government planning. In the latter, there is not any government regulation of the consumption, production, and exchange of goods. Between the two main types lies the mixed economy where market and government are both of importance.

Task 2. Answer the following questions

1. What is central economic problem of the society?
2. What is market?
3. What is the function of the market in an industrial country?
4. How are decisions made in a command economy?

5. In what way does a free market economy differ from a command economy?
6. To which type do most economies in the West belong?

Task 3. Choose correct variant

1. _______ is a society where the government makes all decisions about production and consumption.

a. a command economy
b. a free market economy
c. mixed economy

2._______ studies how markets and prices allow society to solve the problems of what, how and for whom to produce

a. economics

b. economy

c. economical

3. Every economist sees __________ of the question of what, how and for whom to produce
a. the assumption
b. the restriction
c. the importance
4. Nations have different ________ of farm production
a. consumption
b. levels
c. allocation

5. When __________ of some goods grows, people will try to use less of them but producers will want to produce more of them

a. the price

b. the importance

c. the quality

6. In________ countries, Canada and USA, structural changes in the agricultural sector of economy have become of interest to economists and general public in the 80s and 90s of the 20s century

a. second

b. mixed

c. both

7. Economists' recommendations may be of high_________ to governments but governments do not always rely on them

a. valuable
b. value
c. evaluation

8. The study of economics is of great________ even to those students who have no whish to become professional economists

a. use
b. usage
c. usable

9. Grain markets have greatly changed over the last 25 years in the United States and Europe. Both have high levels of government ______________ in the agriculture

a. allocation
b. intervention
c. exploration

10. Resource _________ decisions are being made every bay in every city, mostly through mechanisms of markets and prices

a. taxation
b. allocation
c. intervention

Task 4. Fill in the gaps using the words from the table

Both, government, restrictions, the former, the latter, economics, through, to produce, services(2), goods(2), regulations, mixed economy

1. Every group of people must solve three main problems: what_________ and___________ to produce, how _________ them and for whom to produce them.
2. _________ is placed among the social sciences.
3. Markets in which there is no ________ intervention are called free markets.
4. Society allocates resources into production________ the price system.
5. There are no government_________ and___________ in a free market economy.
6. __________is an economy in which the government and private sector cooperate in solving economic problems.
7. Government regulations and restrictions must _______ work in the interests of society.
8. People produce _________ and __________. ___________ are produced in the factories or in farms, _________ - at schools, hospitals, shops, banks.

Task 5. Match two parts of the sentences

1. America's strong demand for automobiles explains	a. may be called command economies
2. In contrast to market economies, economies with different forms of dictatorial control	b. entirely through government regulation
3. Big corporations are not allowed to dominate an industry or a market	c. and resources are allocated through goods and services markets.
4. In some industries, such as radio, television, telephone services and	d. why auto workers have historically been among the highest paid workers in the world.
	e. which rely heavily on

some others, competition can not be relied 5. Resources are things or services that are used 6. Economics and economists play an important role at the highest levels of governments 7. Until the middle of the 18^{th} century, industry (in contrast to agriculture and commerce) 8. Under capitalism, economic decision-making in decentralized	economic advisers in making decisions about the future of the country. f. entirely on to produce results that are good for the society. g. was of little importance in the economies of Europe and America. h. to produce goods which can satisfy people's demands.

Task 6. Read and translate the text. Fill in the gaps using the words from the box

mixed economy (2)	free market	economic freedom	government	
orders	producer	nationalized	command economy	needs

The________ _________ allows individuals to produce goods and services without any government restrictions. The ___________ ____________allows little individual ___________ ____________since most decisions are made by the government. Between these two extremes lies the ______ ________.

In a ______ ______ the government and private sector co-operate in solving economic problems. The _________ controls production through taxation and ________ for goods and services for the army, the police force, administration and other ________.

In a mixed economy the government may also be a ________ of goods. An example of this is the United Kingdom where there are ____________ industries such as railways and coal.

Task 7. Translate the sentences from Russian into English

1. В странах с рыночной экономикой цены регулируют производство и потребление.
2. Основной целью статьи является формулирование теории о роли правительства в экономической жизни.
3. Экономика изучает то, как общество решает что, как и для кого производить.
4. Во многих странах существует большая степень центрального регулирования и планирования.
5. Развитые страны достигают экономического успеха через специализацию.
6. В годы войны в стране всегда имеет место регулирование экономики правительством.
7. В экономиках смешанного типа имеются правительственные ограничения того, что производить и как производить.
8. Каждый менеджер принимает решения, как распределить ограниченные ресурсы наилучшим образом.

9. Мы не можем положиться на эти данные при планировании производства на следующий год.

10. При рыночной экономике регулирование производства и потребления осуществляется через цены.

UNIT4. FACTORS OF PRODUCTION

Key words: physical capital, financial capital, human capital, fixed capital, circulating capital, labor force, natural resources, purpose, equipment, raw material, available, availability, contribution, means of production, machinery, durable, durable goods, production process, fuel, require, requirement, to meet the requirements, wage, enterprise, non-renewable, to use up, production cycle, value, transfer, final product, investment, efficiency, efficiency of labor, manufacture, management, employment, unemployment, full employment, production costs, population, trade union, job.

Task 1. Read and translate the text.

Factors of Production: Capital and Labor

Factors of production are resources used by firms as inputs for a good or service to be produced. Factors of production are as follows: capital, labor, and natural resources.

In economic theory, the term “capital” refers to goods and money used to produce more goods and money. Classifications of capital vary with the purpose of the classification. The most general distinction is the one made between physical, financial and human capital.

Physical capital is land, buildings, equipment, raw materials; bonds, stocks, available bank balances are included in the financial capital. They both make a great contribution in production.

To group capital into fixed capital and circulating capital is common practice. The former refers to means of production such as land, buildings, machinery and various equipment. They are durable, that is, they participate in the production process over several years. Circulating capital includes both non-renewable goods, such as raw material and fuel, and the funds required to pay wages and other claims against the enterprise. Non-renewable goods are used up in one production cycle and their value is fully transferred to the final product.

Human capital is knowledge that contributes “know-how” to production. It is increased by research and disseminated through education. Investment in human capital results in new, technically improved, products and production process which improve economic efficiency. Like physical capital, human capital is important enough to be an indicator of economic development of a nation.

It is common, in economics, to understand labor as an effort needed to satisfy human needs. It is one of the three leading elements of production. Labor has a variety of functions: production of raw materials, manufacturing of final products, transferring things from one place to another, management of production, and services like the ones rendered physicians and teachers.

One can classify labor into productive and unproductive. The former produces physical objects having utility. The latter is useful but does not produce material wealth. Labor of musician is an example.

Unlike other factors of production, for example capital, once workers are employed, their efficiency can vary greatly with organization of work and their motivation.

Demand for labor is influenced by the demand for goods produced by workers, the proportion of wages in total production costs, etc. The supply of labor depends upon the size of population, geographic mobility, skills, education level (human capital), etc. Workers supply labor either individually or through trade unions. If demand for supply of labor are not in equilibrium, there is unemployment. The rate of unemployment is a percentage of the total labor force without a job. It is desirable for an economy to have the lowest possible unemployment rate and to achieve higher employment as neither full use of resources nor maximum level of output can be achieved in an economy having unemployment.

Factors of production are combined together in different proportions in order to produce output. It is assumed in economics that one should choose the combination of factors which minimizes the cost of production and increases profits.

Task 2. Answer the following questions:

1. Name the factors of production.
2. Characterize factors of production.
3. How is labor classified?
4. What is demand for labor influenced by?
5. How do workers supply labor?

Task 3. Decide if the following statements are true or false:

1. Classifications of capital vary with the purpose of the classification T/F
2. Available bank balances are included in the financial capital T/F
3. Land is not included in the financial capital T/F
4. Fixed capital does not refer to the means of production T/F
5. Circulating capital includes both non-renewable goods, and the funds required to pay wages and other claims against the enterprise T/F
6. The value of non-renewable goods is not fully transferred to the final product T/F
7. Human capital is increased by research and disseminated through education T/F
8. Human capital is an indicator of economic development of a nation T/F
9. Unproductive labor produces physical objects having utility. T/F
10. Demand for labor is not influenced by the demand for goods produced by workers T/F
11. The supply of labor depends upon the education level T/F
12. It is desirable for an economy to have the lowest possible unemployment rate T/F

Task 4. Choose the correct variant:

1.__________ physical capital, human capital is expensive.

a. like

b. unlike

c. both

2. A man's budget constraint is fixed by the total amount of time _____________ over a given period such as a day, a month, a year.

a. following

b. available

c. desired

3. A person has an income which allows him to consume ________ goods and services and live in particular neighbourhood

a. improved

b. efficient

c. various

4. In labor markets many aspects are regulated: paid holidays, the length of working day and week and other aspects of the __________ relationship

a. employment

b. contribution

c. co-workers

5. Changing policies _________ constant updating of statistical systems

a. increase

b. require

c. vary with

6. The activities of trade unions vary from general __________ to specific member's advantages for some jobs

a. protection

b. evaluation

c. internship

Task 5. Match two parts of the sentences

1. Infrastructure equipment…
2. Large Pakistani population living in many countries…

3. Long-term unemployed workers lose…

4. Minimum wages…

5. As to physical capital such as factory and machinery, human capital…

6. It is required that all goods and services…

7. Economists use the word "capital" for goods…

8. The national labor force…

9. Capital includes such non-renewable goods as…

10. Efficiency is…

11. Means of production are…

a. the human capital and contact with the active labor force.
b. the relationship between factor inputs and outputs of goods and services.
c. the same as factors of production.
d. (roads, bridges, telecommunications) is often publicly owned and operated.
e. produced must be bought.
f. includes all people within the nation who are available for work, that is, the working population.
g. sometimes reduce the demand for labor.
h. raw materials and fuel.

i. that are not entirely used up in the production process.
j. regularly transfers labor income to the home country.
k. is the result of past investment and its purpose is to generate future incomes.

Task 6. Fill in the gaps using the words from the box.

referred both…and, to contribute, to employ, employment, unlike, variety, purpose, machinery, available, various

1. As productive equipment is __________ to as physical capital, to buy new equipment is to invest in production.

2. _________ physical capital, human capital does not belong to the firm that has invested in it.

3. Trade union restrictions do not allow __________ of youth in some industries and many service sectors.

4. The________ of minimum wages is to protect young people from exploitation.

5. The European Union's statistics are collected___________ at the union level_______ at national levels of member countries.

6. There are _________ forms of money.

7. Natural resources research in the USA of the 1930s was based on gathering information from a __________ of sources.

8. The marginal product of labor shows how much each additional worker increases total output. The marginal product grows as the first few workers are _______ because it is hard for the first and second worker to handle all the _______. By the time the third worker is _________, marginal productivity of labor starts falling. When all __________ machines are fully used, each new worker has less and less to __________.

Task 7. Translate the sentences from Russian into English

1. Важно производить конечный продукт на территории страны.
2. Трудовые ресурсы – это часть населения, участвующая в производстве.
3. Труд имеет следующие основные функции: производство сырья, промышленное производство конечного продукта, управление и услуги.
4. Основные факторы производства следующие: земля, техника, финансовый капитал и труд.
5. Предприятие – это единица производства и управления.
6. В начале 90-х годов 40% трудовых ресурсов России было занято в негосударственном секторе экономики.
7. Повышение цен на нефть в начале 1970-х годов было достаточно сильным. Чтобы вызвать немедленное повышение стоимости экспорта топлива.

UNIT 5. DEMAND AND SUPPLY

Task 1. Read and translate the text.

Key words: quantity, demand, supply, excess supply, equilibrium price, producer, consumer, shortage, raise, surplus, reduce, influence, income, increase, substitute good, decrease, complement good, normal good, inferior good, fall, input price, improvement, impose.

History

The phrase "supply and demand" was first used by James Denham-Steuart in his ***Inquiry into the Principles of Political Economy***, published in 1767. Adam Smith used the phrase in his 1776 book ***The Wealth of Nations***, and David Ricardo titled one chapter of his 1817 work ***Principles of Political Economy and Taxation*** **"On the Influence of Demand and Supply on Price"**.

In ***The Wealth of Nations***, Smith generally assumed that the supply price was fixed but that the demand would increase or decrease as the price decreased or increased. Ricardo, in ***Principles of Political Economy and Taxation***, more rigorously laid down the idea of the assumptions that were used to build his ideas of supply and demand. Antoine Augustin Cournot first developed a mathematical model of supply and demand in his 1838 ***Researches on the Mathematical Principles of the Theory of Wealth.***

During the late 19th century the marginalist school of thought emerged. This field mainly was started by Stanley Jevons, Carl Menger, and Léon Walras. The key idea was that the price was set by the most expensive price, that is, the price at the margin. This was a substantial change from Adam Smith's thoughts on determining the supply price.

The model was further developed and popularized by Alfred Marshall in the 1890 textbook ***Principles of Economics***. Along with Léon Walras, Marshall looked at the equilibrium point where the two curves crossed. They also began looking at the effect of markets on each other. Since the late 19th century, the theory of supply and demand has mainly been unchanged. Most of the work has been in examining the exceptions to the model (like oligarchy, transaction costs, non-rationality).

General definitions

Demand is the quantity of a good that buyers wish to buy at each price. Other things equal, at low prices the demanded quantity is higher.

Supply is the quantity of a good that sellers wish to sell at each price. Other thing equal, when prices are high, the supplied quantity is high as well.

The market is in equilibrium when the price regulates the quantity supplied by producers and the quantity demanded by consumers. When prices are not so high as equilibrium price, there is excess demand (shortage) raising the price. At prices above equilibrium price, there is excess supply (surplus) reducing the price.

There are some factors influencing demand for a good, such as the prices of other goods, consumer incomes and some others.

An increase in the good of a substitute good (or a decrease in the price of a complement good) will at the same time raise the demanded quantity.

As consumer income is increased, demand for a normal good will also increase but demand for an inferior good will decrease. A normal good is a good for which demand increases when incomes rise. An inferior good is a good for which demand falls when incomes rise.

As to supply, some factors are assumed as constant. Among them are technology, the input price, as well as degree of government regulation. An improvement in technology is as important for increasing the supplied quantity of a good as a reduction in input prices.

Government regulates demand and supply, imposing ceiling prices (maximum prices) and floor prices (minimum prices) and adding its own demand to the demand of the private sector.

Task 2. Answer the following questions.

1. Who used the term "supply and demand" for the first time?
2. What did Smith assume?
3. What did Antoine Augustin Cournot develop?
4. What was the key idea of the marginalist school?
5. What did Alfred Marshall study?
6. What is demand?
7. What is supply?
8. Describe the interrelationship between the quantity supplied by producers and the quantity demanded by consumers.
9. What factors influence demand for a good?
10. What raises the demanded quantity?
11. When does the demand for a normal good increase?

12. Give the definitions for such terms: *a normal good, an inferior good.*
13. What factors influence supply ?
14. In what way does the government regulate demand and supply?

Task 3. Decide if the following statements are true or false.

1. The phrase "supply and demand" was first used by Adam Smith in his 1776 book ***The Wealth of Nations.*** T/F
2. Ricardo, in ***Principles of Political Economy and Taxation***, laid down the idea of the assumptions that were used to build his ideas of supply and demand. T/F
3. A mathematical model of supply and demand was firstly developed 1838 T/F
4. The marginalist school of thought emerged in the 18^{th} century T/F
5. Since the late 19th century, the theory of supply and demand has been greatly changed T/F
6. Demand is the quantity of a good that buyers wish to buy at low prices T/F
7. Supply is the quantity of a good that sellers wish to sell at each price T/F
8. When prices are not so high as equilibrium price, there is excess supply (surplus) reducing the price T/F
9. At prices above equilibrium price, there is excess demand (shortage) raising the price T/F
10. An increase in the price of a substitute good will reduce the demanded quantity T/F
11. A normal good is a good for which demand increases when incomes rise. T/F
12. An inferior good is a good for which demand rises when incomes rise. T/F
13. As consumer income is increased, demand for a normal good will also increase but demand for an inferior good will decrease. T/F
14. Government does not regulate demand and supply. T/F

Task 4. Fill in the gaps using the words from the box

High important(2) many large low effectively much great clear reliable strong (2) quickly

1. Command economy relies________on planning than on prices.
2. Knowledge of foreign languages is of ________ importance now than it was some 40 years ago.
3. The degree of government regulation in present-day Ukraine is ___________ than in the Soviet Union.
4. Government regulation in Sweden is as ___________as in Denmark or, probably,_______.
5. Land quality is ____________ for agriculture than for other industries.
6. If we want to have a __________ of economic life in the country, we must have____________ information.
7. In the 18th century the ____________ part of national income in _________European countries came from import and export tariffs. These days they play a ______ role.
8. Governments can influence for whom goods are produced __________ in economies with ____________ levels of government regulation.
9. If other things are equal, this firm will do the work _______ than the others.

Task 5. Match two parts of the sentences

1. In East-European countries consumers couldn't get goods, and factories couldn't buy inputs 2. Governments intervene in economies controlling the supply of money, 3. An improvement in	a. telling suppliers it is now time to increase production. b. limiting monopolies and helping private business. c. increasing the quantity supplied at each possible price. d. at prices held low by

technology will increase the supply of a good, 4. Governments regulate economic activities 5. The governments can influence for whom the goods are produced, 6. The high price for a good is the market mechanism	governments. e. imposing some restrictions. f. taking income away from some people and giving it to others

Task 6. Choose the correct variant

1. The fashion for mini-skirt__________ the demand for textile materials

a. increased
b. reduced
c. didn't change

2. Even in________ middle-income countries many people are very poor

a. some
b. any
c. the same

3. Stabilization of prices is of great importance to industrial nations________the Third World countries

a. as well as
b. than
c. as well

4. Freeing up prices leads to their ___________

a. decrease
b. increase
c. stabilization

5. __________ goods are usually low-quality goods for which there are higher-quality substitutes sold at higher prices

a. luxurious
b. inferior
c. normal

6. A decrease in ________ prices makes the production less expensive

a. complement
b. input
c. inferior

Task 7. Translate the sentences from Russian into English

1. По мере того как цена товара растет, требуемое количество его уменьшается.
2. Положение в странах с низким доходом улучшилось с 1965 года.
3. Задача максимальной цены состоит в том, чтобы уменьшить цену для потребителей, а задача минимальной цены заключается в том, чтобы поднять цену для производителей и поставщиков.
4. Увеличение предложения ведет к повышению равновесного количества и понижению равновесной цены.
5. Когда цены будут уменьшены до равновесной цены, не будет товарных излишков.
6. Если цена одного товара падает, а цены других товаров, требуемых потребителем, остаются теми же самыми, то потребитель будет покупать более дешевые товары вместо дорогого товара.

Task 8. Read the text and fill in the gaps using the words from the box

Amount(2)	shortage	fall	vary	equilibrium	inversely	intersection
equal	proportional					

The model asserts that in a free market, the_________ of a product supplied by the producer and the ______ demanded on the consumer are dependent on the market price of the product. The **law of supply** states that supply is directly__________ to price; the higher the price of the product, the more the producer will supply. The **law of demand** states that demand is__________ proportional to price; the higher the price of the product, the less the consumer will demand. Thus, supply and demand both_________ with price.

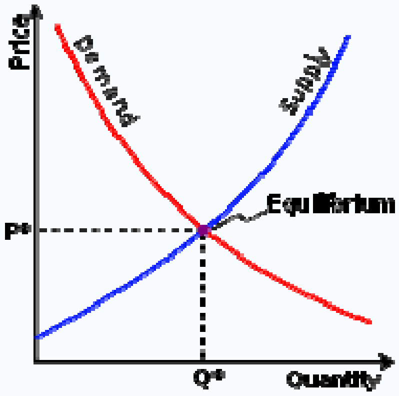
The **law of supply and demand** states that the market price of a good is the____________ of consumer demand and producer supply. If the price for a good is at a low level where consumers demand more of the good than producers are prepared to supply, there will be a________ of the good, and consumers will be willing to pay more for it. The producers will increase the price until it reaches the level where consumers would not buy any more if the price was increased. Conversely, if the price for a good is at a high level where the suppliers would like to produce more than the consumers will buy, the producers will be willing to lower the price. The price will________ until it reaches the level where consumers would be willing to pay more for the good.

This point to which prices will move towards is the point of economic________ , where the quantity supplied is________ to the quantity demanded — producers are prepared to sell exactly the same quantity of goods as the consumers want to buy.

Task 9. Read and translate the text

Simple supply and demand curves

Economic theory centers on creating a series of supply and demand relationships, describing them as equations, and then adjusting for factors which produce "stickiness" between supply and demand. Analysis is then done to see what "trade offs" are made in the "market", which is the negotiation between sellers and buyers. Analysis is done as to what point the ability of sellers to sell becomes less useful than other opportunities. This is related to "marginal" costs, or the price to produce the last unit that can be sold profitably, versus the chance of using the same effort to engage in some other activity.



The slope of the demand curve (downward to the right) indicates that a greater quantity will be demanded when the price is lower. On the other hand, the slope of the supply curve (upward to the right) tells us that as the price goes up, producers are willing to produce more goods. The point at which these curves intersect is the equilibrium point. At a price of P* producers will be willing to supply Q* units per period of time and buyers will demand the same quantity. P* in this example, is the equilibrating price that equates supply with demand.

In the figures, straight lines are drawn instead of the more general curves. This is typical in analysis looking at the simplified relationships between supply and demand because the shape of the curve does not change the general relationships and lessons of the supply and demand theory. The shape of the curves far away from the equilibrium point are less likely to be important because they do not affect the market clearing price and will not affect it unless large shifts in the supply or demand occur. So straight lines for supply and demand with the proper slope will convey most of the information the model can offer. In any case, the exact shape of the curve is not easy to determine for a given market. The general shape of the curve, especially its slope near the equilibrium point, does however have an impact on how a market will adjust to changes in demand or supply.

It should be noted that on supply and demand curves both are drawn as a function of price. Neither is represented as a function of the other. Rather the two functions interact in a manner that is representative of market outcomes. The curves also imply a somewhat neutral means of measuring price. In practice any currency or commodity used to measure price is also the subject of supply and demand.

Task 10. Answer the following questions

1. What does the slope of demand curve indicate?
2. What does the slope of supply curve indicate?
3. What is equilibrium point?

UNIT 6. THEORY OF DEMAND

Task 1. Read and translate the text

Key words: consumer demand, constant, relationship, assume, assumption, budget constraint, utility, marginal utility, prefer, obtain, provided, maintain, follow, additional, unit, expenditure, market demand, depend upon, affect.

Theory of Demand

Consumer demand is the quantities of a particular good that an individual consumer wants and is able to buy as the price varies, if all other factors influencing demand are constant.

That is, consumer demand is the relationship between the quantity demanded for the good and its price. The factors assumed constant are the prices of other goods, income and a number of non-economic factors, such as social, physiological, demographic characteristics of the consumer in question.

The theory of demand is based on the assumption that the consumer having budget constraint seeks to reach the maximum possible level of utility, that is, to maximize the utility, but he usually prefers to obtain more rather than less. The consumer has to solve the problem of choice. Provided he is to maintain a given level of utility, increases in the quantity of one good must be followed by reductions in the quantity of the other good. The consumer has to choose the specific goods within the limits imposed by his budget.

The concept of marginal utility is of great importance for solving the utility maximization problem. The marginal utility of a good is the additional utility obtained from consuming an additional unit of the good in question. The marginal utility from consuming a good decreases as more of that good is consumed. The income should be allocated among all possible choices so that the marginal utility per dollar of expenditure on each good is equal to the marginal utility per dollar of expenditure on every other good.

A price increase will result in a reduction in the quantity demanded. This relationship between the quantity demanded of a good and its price is called the low of demand. As the marginal utility from each additional unit of the good consumed decreases, the consumer will want to buy more of this good only if its price is reduced.

Market demand is the quantities of a good that all consumers in a particular market want and are able to buy as price varies and all other factors are assumed constant. Market demand depends not only on the factors affecting individual demands, but also on the number of consumers in the market. The law of demand also works with market demand.

Task 2. Answer the following questions

1. What is consumer demand?
2. What factors influencing consumer demand are assumed constant?
3. What is the principal assumption of the demand theory?
4. What choice does the consumer have to make?
5. What is marginal utility?
6. How should the consumer allocate his income?
7. How does the marginal utility change as the consumption of a good increases?
8. What is market demand?
9. In what way is the marginal utility connected with price?
10. In what way does market demand differ from individual demand?

Task 3. Decide if the following statements are true or false

1. Consumer demand is the quantities of a particular good that an individual consumer wants and is able to buy at constant prices T/F
2. Consumer demand is the relationship between the quantity demanded for the good and its price T/F
3. The consumer having budget constraint seeks to reach the maximum possible level of utility T/F
4. Provided the consumer is to maintain a given level of utility, reductions in the quantity of one good must be followed by reductions in the quantity of the other good T/F
5. The marginal utility of a good is the additional utility obtained from consuming an additional unit of the good in question T/F
6. The marginal utility from consuming a good increases as more of that good is consumed T/F
7. A price increase will result in a reduction in the quantity demanded T/F
8. Market demand depends only on the factors affecting individual demands T/F

Task 4. Fill in the gaps using the words from the box

Choice, to obtain (2), number, that is, within (2), to maintain, constant, rather than, per(4), provided, to result in, to assume, to choose

1. We assume that the consumer prefers to have more of a good _____ _____ less.
2. _______ the good whose price has risen is a normal good, the economist can ________ that the demand for it will fall.
3. A constant level of utility is ________ through correct choice of goods or services that can be _________ at one time.

4. The lower price ________ ___________ additional demand.
5. People must often make a _________ between two or more goods. They usually _________ the good with the highest utility _______ limited budget, _________ __________, choose the cheapest good.
6. Income is usually counted _________ year, but sometimes also __________ month or even _________ week.
7. The man having a credit card has to pay ________ a certain ________ of days for everything that he has bought with its help during the month.
8. We do not assume that _________ acre productivity will remain _______ as modern agricultural technology allows farmers to ________ better results.

Task 5. Choose correct variant

1. An increase in food prices greatly _______ consumer real income because food is a large part of consumer expenditure

a. affects
b. follows
c. imposes

2. An increase in the price of the good ***j*** increases the quantity demanded of the good ***i*** when the two goods are ________ but reduces the quantity demanded of the good ***i*** when the two goods are complements

a. inferior
b. substitutes
c. normal

3. We ________ that the consumer always decides that one good is better than, worse than, or as good as another.

a. prefer
b. assume
c. sum up

4. This model of consumer ________ can show different behaviour of different consumers

a. goods
b. expenditure
c. choice

5. The demand theory assumes that the consumer ________ on a budget constraint wants to maximize utility

a. following
b. assuming
c. depending

6. Importers often must first _________ an import licence

a. follow
b. obtain
c. find

7. Economic development is the process of raising the income ______

a. per
b. for
c. within

8. If the level of imports is high, great parts of incomes are spent on the goods produced abroad__________ on the goods produced at home

a. that is
b. over
c. rather than

9. Statistics show that the ________ of working women with young children is constantly growing in the USA today

a. character
b. the budget constraint
c. the number

11. An increase in consumer expenditure usually ________ an equivalent rise in the income of consumers

a. follows

b. results

c. increases

12. The problem of the consumer is to choose the particular goods and services within the limits__________ by his budget

a. imposed

b. allocated

c. produced

Task 6. Match two parts of the sentences

1. Increase in the utility of one good can compensate 2. Equilibrium price is the price at which 3. The marginal utility of a good is the increase in 4. There are different ways 5. Over 60 per cent of the capital of all US firms is in agro-industry 6. Higher expenditure on foreign goods rather than on goods produced at home 7. Rising incomes result in 8. Per capital income in the united States	a. the quantity demanded is equal to the quantity supplied b. to restrict import expenditure c. that is, industry based on agricultural products d. an absolute fall of demand for inferior goods e. is still higher than in Japan f. the utility obtained by consuming one more unit of that good g. the reduction of utility of another good h. will increase demand for foreign goods

Task 7. Translate the sentences from Russian into English

1. Когда цена на один товар возрастает, потребитель покупает товар, цена которого не возросла.

2. Принимая решение, экономист должен полагаться на любую информацию, которую он может найти.
3. Сокращение доходов приводит в повышенному спросу на товары низкого качества.
4. Предельная полезность зависит от количества потребленных товаров.
5. Потребитель всегда стремиться приобретать товар, который предоставляет ему больше предельной полезности на каждый потраченный доллар.
6. Каждый потребитель должен решить проблему выбора.
7. При равновесной цене предложение равно спросу.
8. Цены ниже равновесной приводят к дефициту.
9. На свободном рынке изменения цены зависят от изменения спроса и предложения.
10. Фирма может контролировать одну или более производственных единиц.
11. Концепция предельной полезности очень важна для решения некоторых проблем спроса.

Task 8. Read and translate the text. Fill in the gaps using the words from the box

Purchasing	distribution	the same	equal	represents
purchase	phenomenon	tastes	complementary	explained

Demand schedule

Demand is economic want backed up by__________ power. The demand schedule, depicted graphically as the demand curve,________ the amount of a good that buyers are willing and able to________ at various prices, assuming all other non-price factors remain_______. The demand curve is almost always downwards-sloping, meaning that as price increases, consumers will buy less of a good.

Just as the supply curves are________ to marginal cost curves, demand curves are equal to marginal utility curves.

The main determinants of individual demand are the price of the good, level of income, personal ________, the price of substitute goods, and the price of________ goods.

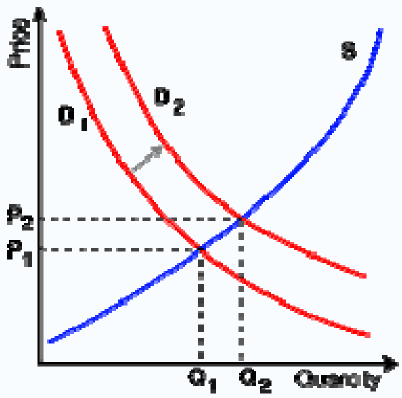
The shape of the aggregate demand curve can be convex or concave, possibly depending on income____________.

As described above, the demand curve is generally downward sloping. There may be rare examples of goods that have upward sloping demand curves. A good whose demand curve has an upward slope is known as a Giffen good or Veblen good.

The existence of Giffen goods cannot be_________ by conspicuous consumption, since an increase in stature associated with buying an expensive product means that more than just price is variable. In fact the actual existence of a Giffen good is debatable. Examples of conspicuous consumption are clearly subjective, but might include the Bugatti Veyron. The social_________ often referred to as 'Bling' can also be thought of in this way.

Task 9. Read and translate the text, answer the questions

Demand curve shifts



An out- or right- shift in demand changes the equilibrium price and quantity

When more people want something, the quantity demanded at all prices will tend to increase. This can be referred to as an increase in demand. The increase in demand could also come from changing tastes, where the same consumers desire more of the same good than they previously did. Increased demand can be represented on the graph as the curve being shifted right, because at each price point, a greater quantity is demanded. An example of this would be more people suddenly wanting more coffee. This change in consumer preferences will cause the curve to shift (to the right) from the initial curve D1 to the new curve D2. This raises the equilibrium price from P1 to the higher P2. This raises the equilibrium quantity from Q1 to the higher Q2. In this situation, we say that there has been an increase in demand which has caused an extension in supply.

Conversely, if the demand decreases, the opposite happens. If the demand starts at D2 and then decreases to D1, the price will decrease and the quantity demanded will decrease—a contraction in supply. Notice that this is purely an effect of demand changing. The quantity supplied at each price is the same as before the demand shift (at both Q1 and Q2).

Answer the questions:

1. What factors influence demand?
2. What rises equilibrium price and equilibrium quantity?
3. What happens when demand decreases?

UNIT 7. THE THEORY OF SUPPLY

Task 1. Read and translate the text

Key words: output, profit, revenue, marginal revenue, costs, marginal costs, opportunity costs, earn, expenses, include, commodity, amount, alternative, corresponding, own.

The theory of supply is the theory of how much output firms choose to produce. The principal assumption of the supply theory is that the producer will maintain the level of output at which he maximizes the profit.

Profit can be defined in terms of revenue and costs. Revenue is what the firm earns by selling goods and services in a given period such as a year. Costs are the expenses which are necessary for producing and selling goods or services during the period. Profit is the revenue from selling output minus the costs of inputs used.

Costs should include opportunity costs of all resources used in the production. Opportunity cost of a commodity is the amount an input can obtain in the best alternative use (best use elsewhere). In particular, costs include the owner's time and effort in running a business. Costs also include the opportunity cost of the financial capital used in the firm.

Aiming to get higher profits, firms obtain each output level as cheaply as possible. Firms choose the optimal output level to receive the highest profits. This decision can be described in terms of marginal cost and marginal revenue.

Marginal cost is the increase in total cost when one additional unit of output is produced.

Marginal revenue is the corresponding change in total revenue from selling one more unit of output.

As the individual firm has to be a price-taker, each firm's marginal revenue is the prevailing market price. Profits are the highest at the output level at which marginal cost is equal to marginal revenue, that is, to the market price of the output. If the profits are negative at this output level, the form should close down.

An increase in marginal cost reduces output. A rise in marginal revenue increases output. The optimal quantity also depends on the output prices as well as on the input costs. Of course, the optimal supply quantity is affected by such non-economic factors as technology, environment, etc.

Making economic forecasts, it is necessary to know the effect of a price change on the whole output rather than the supply of individual firms.

Market supply is defined in terms of the alternative quantities of a commodity all firms in a particular market offer as price varies and as all other factors are assumed constant.

Task 2. Answer the following questions:

1. What is the principal assumption of the supply theory?
2. What is the difference between profit and revenue?
3. What is included in costs of production?
4. How do firms get maximum profits?
5. When are the profits the highest?
6. When should firms close down?
7. What is the relationship between marginal revenue, marginal cost and output?
8. What is market supply? What is market supply important for?

Task 3. Decide if the statements are true or false

1. The principal assumption of the supply theory is that the producer will maintain the level of output at which he maximizes the profit. T/F
2. Costs are what the firm earns by selling goods and services in a given period such as a year. T/F
3. Revenue is the expenses which are necessary for producing and selling goods or services during the period. T/F
4. Profit is the revenue from selling the output minus the costs of inputs used. T/F
5. Opportunity cost of a commodity is the amount an input can obtain in the best alternative use. T/F
6. Firms obtain each output level as cheaply as possible. T/F
7. If the profits are negative at this output level, the form should close down. T/F

8. Marginal cost is the decrease in total cost when one additional unit of output is produced. T/F
9. An increase in marginal cost expands output. T/F
10. The optimal supply quantity is affected by such non-economic factors as technology and environment. T/F

Task 4. Match two parts of the sentences

1. Market demand is 2. An improvement in technology 3. Profits are 4. As long as the total demand and the total supply of the commodity remain equal, 5. Part of a company's profits is put back into the business rather than 6. examining how revenues and costs change with the level of output produced and sold, 7. With inflation, people have to increase expenditure because 8. Profit depends on 9. Opportunity cost is the amount	a. revenues minus cots. b. the firm can select the output level maximizing its profit. c. paid out as dividends. d. the equilibrium price will remain unchanged. e. makes it possible for firms to produce more goods with the same amount of resources as before. f. how much the amount received is greater than the amounts paid. g. the total demand from all consumers. h. the old level of expenditure in money terms now buys a smaller quantity of goods. i. an input can obtain in its use elsewhere

Task 5. Choose correct variant

1. Farmers may__________ more revenue from a bad harvest than from a good harvest

a. own
b. earn
c. run

2. A rise in the income of consumers will typically result in an equivalent increase in ____________ consumer expenditure

a. corresponding
b. total
c. alternative

3. Statistics show the greatest increase in the number of jobs in the American non-production sector among government workers __________ today

a. in terms of
b. elsewhere
c. in particular

4. Do not forget to calculate the _________ of the man's labour, that is, the money that he could earn by working elsewhere

a. marginal cost
b. costs
c. opportunity costs

5. In Marxist theory, proletarist is the social class of workers who have to see their __________ ability to work

a. corresponding
b. own
c. total

6. If we want to understand how firms make output decisions, we must analyze how they determine _________

a. revenues
b. output
c. amounts

7. Higher _________ have much more influence on the way people eat (more meat, less bread) than on the amount they eat

a. incomes
b. education
c. experience

8. The price at the time the good is ready for marketing may be _______ from the price at the time the decision to produce it was made

a. equal
b. corresponding
c. different

9. Real _______ is the amount of the goods and services a consumer can buy with his money income

a. income
b. tax
c. revenue

10. ________ is the amount of a good that will be offered in the market at a certain price and time

a. profit
b. supply
c. revenue

Task 6. Fill in the gaps using the word from the box

opportunity cost, corresponding, profit, owner, to own, to use (2), alternative, expenses, own, marginal costs, marginal revenue, allotting, boom

1. The syndicate controls prices and output and, _________ quotas to its members, it divides the market demand among them.
2. _________ is a period of increased business activity when a rising demand for all commodities results in increased industrial production.
3. A free market is a market in which buyers and sellers are free of intervention and control and are able to determine the market price _________ to supply and demand.
4. A person is economically free if he can do what he wishes with its his ________ property, time and effort.

5. The personal sector in a mixed economy is that part of the economy that is __________ and controlled by private persons and private businesses.
6. The main aim of all firms is the same: to maximize __________ though there may be __________aims as well.
7. Under feudal system the king was the ___________ of all land, and his lords could _________ his land. The system came into an end when the peasants were paid for their work and paid rent for the lend they________.
8. ______ ______ is the amount lost by not using the resource (labour and capital) in its best alternative use.
9. At profit-maximizing level ________ _________ has to be equal to ______ ________.
10. Profit is the difference between business income and______.

Task 7. Translate the sentences from Russian into English

1. Потребитель – это человек, потребляющий продукты и услуги.
2. Производитель всегда стремиться поддерживать уровень производства, при котором он максимизирует прибыль.
3. Стремясь получить более высокую прибыль, производители используют дешевые ресурсы.
4. Рыночный спрос – это общий спрос на товар в обществе.
5. не все партнеры в деле должны принимать активное участие в управлении фирмой.
6. Нелегко рассчитать доход, издержки и прибыли для большого предприятия.
7. Фермер – это человек, который владеет и управляет фирмой.
8. Когда цена поднимается выше предельных издержек, каждый производитель хочет производить больше.
9. Даже при нулевой выработке фирма должна оплачивать некоторые расходы.

10. Издержки должны включать альтернативные издержки всех ресурсов, используемых в производстве.

Task 8. Read and translate the text, answer the questions.

Supply schedule

The supply schedule is the relationship between the quantity of goods supplied by the producers of a good and the current market price. It is graphically represented by the supply curve. Since supply is generally directly proportional to price, supply curves are almost always upwards-sloping. Also, the slope of a supply curve is usually increasingly upwards-sloping (i.e., the curve is a convex function) due of the law of diminishing marginal returns.

The supply curve for a given producer is equal to the producer's marginal cost curve because of the equimarginal principle. Thus, the supply curve for the entire market can be expressed as the sum of the marginal cost curves of the individual producers.

Occasionally, supply curves do not slope upwards. A well known example is the backward bending supply curve of labour. Generally, as a worker's wage increases, he is willing to supply a greater amount of labor (working more hours), since the higher wage increases the marginal utility of working (and increases the opportunity cost of not working). But when the wage reaches an extremely high amount, the laborer may experience the law of diminishing marginal utility in relation to his salary. The large amount of money he is making will make further money of little value to him. Thus, he will work less and less as the wage increases, choosing instead to spend his time in leisure. The backwards-bending supply curve has also been observed in non-labor markets, including the market for oil: after the skyrocketing price of oil caused by the 1973 oil crisis, many oil-exporting countries decreased their production of oil.

Another example of a nontraditional supply curve is the supply curve for utility production companies. Because a large portion of their total costs are in the form of fixed costs, the marginal cost (supply curve) for these firms is often depicted as a constant.

Another postulated variant of a supply curve is that for child labor. Supply will increase as wages increase, but at a certain point a child's parents will pull the child from the child labor force due to cultural pressures and a desire to concentrate on education. The supply will not increase as the wage increases, up to a point where the wage is high enough to offset these concerns. For a normal demand curve, this can result in two stable equilibrium points - a high wage and a low wage equilibrium point.

Questions:

1. What is supply schedule?
2. Explain the slope of supply curve.
3. What is supply curve equal to?
4. Give examples of a nontraditional supply curve.

UNIT 8. INFLATION

Key words: steady, inflationary spiral, inflation rate, hyperinflation, cause, explain, account, accept, occur, ensure, incomes policy, argue, speed, anticipate, extent, adjustment, indexation, cope with

Task 1. Read and translate the text.

Inflation

Inflation is a steady rise in the average price and wage level. The rise in wages being high enough to rise costs of production, prices grow further resulting in a higher rate of inflation and, finally, in an inflationary spiral. Periods when inflation rates are referred to as hyperinflation.

The causes of inflation are rather complicated, and there is a number of theories explaining them. Monetarists, such as Milton Friedman, say that inflation is caused by too rapid increase in money supply and the corresponding excess demand for goods.

Therefore, monetarists consider due government control of money supply to be able to restrict inflation rates. They also believe the high rate of unemployment to be likely to restrain claims for higher wages. People having jobs accept the wages they are being paid, the inflationary spiral being kept under control. This situation also accounts for rather slow increase in aggregate demand.

On the other hand, Keynesians, that is, economists following the theory of John M.Keynes, suppose inflation to be due to process occurring in money circulation. They say that low inflation and unemployment rates can be ensured by adopting a tight incomes policy.

Incomes policies, though, monetarists argue, may temporarily speed up the transition to a lower inflation rate but they are unlikely to succeed in the long run.

The costs of inflation depend on whether it was anticipated and on the extent to which the economy’s institutions allow complete inflation adjustment.

The longer inflation continues, the more the economy learns to live with it. Indexation is a means to reduce the costs of some inflation effects. Indexed wages or loans mean that the amount to be paid or repaid will rise with the price level. Indexation has already been introduces in countries that had to live with inflation rates of 30 or 40 per cent for years. And the more countries adjust their economies to cope with the inflation, the closer they come to hyperinflation. Indexation means that high rates of inflation are much more likely to continue and even to increase.

Task 2. Answer the following questions:

1. What is inflation?
2. What is hyperinflation?

3. Characterize the causes of inflation.
4. What do the costs of inflation depend on?
5. What is indexation?

Task 3. Decide if the following statements are true or false.

1. Prices grow results in a higher rate of inflation. T/F
2. Hyperinflation is a steady rise of inflation rates. T/F
3. Monetarists believe that inflation is caused by too slow increase in money supply. T/F
4. Monetarists suppose the low rate of unemployment to be likely to restrain claims for higher wages. T/F
5. Keynesians suppose inflation to be due to process occurring in money circulation. T/F
6. Monetarists believe incomes policies may temporarily slow up the transition to a lower inflation rate. T/F
7. Indexation is a means to reduce the costs of some inflation effects. T/F
8. Indexed wages or loans mean that the amount to be paid or repaid will fall with the price level. T/F
9. The more countries adjust their economies to cope with the inflation, the closer they come to hyperinflation. T/F
10. Indexation means that high rates of inflation are much more likely to continue and even to increase.

Task 4. Choose the correct variant.

1.In the United Kingdom in the 1970s the Labour government tried to reduce the difference between high-wage jobs by ___________ an incomes policy that allowed an absolute rather than a percentage increase

a. adopting
b. arguing
c. evaluating

2. Pensions and other payments are raised every year by the rate corresponding to the rate of _________ inflation

a. any

b. anticipated

c. studied

3. Taxing the rich and transferring the funds to the poor, the government ___________ that the poor get more of what is produced

a. produces

b. adjusts

c. ensures

4. Without __________ it is costly to live with high inflation rates

a. means

b. funds

c. indexation

5. In practice the distinction between land and capital is _________ uncertain

a. though

b. rather

c. a bit

6. The output of new ideas depends to a large ________ on the resources allocated for them

a. quantity

b. extent

c. number

7. Producing output, any firm uses the cheapest _______ technique

a. available

b. fixed

c. introduced

8. With slow price and wage adjustment, an ___________ in money supply results in a temporary output rise, but eventually it only causes higher prices

a. increase

b. decrease

c. development

9. Governments and political parties usually have to decide whether they like the ________ of income caused by inflation

a. realization

b. redistribution

c. evaluation

10. __________ means that the wages agreement will remain correct for any anticipated inflation that occurred over the life of the contract

a. hyperinflation

b. indexation

c. taxation

Task 5. Fill in the gaps using the words from the box

therefore, eventually, as a result (2), in particular, on the one hand, on the other hand, as, actually, that is, both…and…,unlike, whereas

Hyperinflation is a situation of high rates of inflation. __________ creeping inflation, … … small but steady increases in the level of prices, which usually has little bad effect on the economy as a whole, hyperinflation makes people loose confidence in the value of money to such an extent that they start using barter. _________ __________ _________, there is a serious danger of economic collapse and, ________, of social trouble. ___________, the costs of hyperinflation are said to be very high.

_____ _______ _______ ______, hyperinflation does not occur often, but when it does occur, its causes are much political as economic. It occurs _______ _______ ________ of a great increase of money in money supply to finance government spending (during wars, _______ _______). _________ _______ _______ ________, hyperinflation can result from shortage of goods and services alongside great demand for them, _______ in periods following the ending of a war.

Task 6. Translate the sentences from Russian into English.

1. Ускорение денежного обращения вызывает более высокие темпы инфляции.
2. В индустриальных странах доля наличных денег составляет до 4% денежной массы в обращении.
3. Политика доходов – это попытка прямо повлиять на заработную плату и другие доходы.
4. Когда повышается темп инфляции, процентные ставки растут, а совокупный спрос падает.
5. Экономисты уже определили, что вызывает инфляцию.
6. Правительство может принять жесткую политику, которая должна обеспечить низкий темп инфляции.
7. Постоянное увеличение денежной массы должно вызвать инфляцию.

UNIT 9. TAXATION

Task 1. Read and translate key words: taxation, national defence, to levy the tax, to expand, revenue, taxpayer, voter, property tax, transaction, direct tax, income tax, capital gains, excise tax.

Task 2. Read and translate the text.

TAXATION

Taxation is a system of raising money to finance government services activities. Governments at all levels - local, provincial, and national require people and business to pay taxes. Governments use the tax revenues to pay the cost of police and fire protection, health programmes, schools, roads, national defence, and many other public services. Direct taxes are levied (charged) on the incomes or wealth of individuals or companies.

Taxes are as old as government. The general level of taxes has varied over the years, depending on the role of the government. In modern times, many governments - especially in advanced industrial countries - have rapidly expanded their roles and taken on new responsibilities. As a result, their need for tax revenue has increased.

Over the years, people have frequently protested against tax increases. In these situations, taxpayers have favoured keeping services at current levels or reducing them. Voters have defeated many proposals for tax increases by provincial and local governments.

Governments levy many kinds of taxes. The most important kinds include property taxes, income taxes on transaction.

Property taxes are levied on the value of such property as houses, shops, factories, farms, and business equipment. The property tax first became important in ancient times. Today, it ranks as the chief source of income for many local governments. Property taxes are known as rates in some countries. They are called direct taxes because they are levied directly on the people expected to pay them.

Income taxes are levied on income from such sources as wages and salaries, dividends, interest, rent, and earning of companies. There are two main types of income taxes - individual income taxes and corporate income taxes. Individual income taxes, also called personal income taxes, are applied to the income of individuals and families. Corporate income taxes are levied on earnings of companies or corporations. Income taxes may also be levied on the earnings of estates and trusts. They generally are considered to be direct taxes. The corporate income tax also may be described as shifted tax. This is because companies shift the cost of the tax to their customers by raising prices. Most nations in the world levy income taxes. Many people have income tax deducted automatically from their earnings by employers, who then pay it to the tax office.

Capital gains tax is a tax, separate from income tax, levied on profits received from the sale or exchange of real property, shares or other assets. If losses are made on some sales, they can be subtracted from overall profits to work out the amount liable to capital gains tax. Some countries treat capital gains as ordinary income, and charge income tax on them.

Taxes on transactions are levied on sales of goods and services and on privileges. There are three main types of such taxes - general sales taxes, excise taxes, and tariffs.

General sales taxes apply one rate to the sales of many different items. Australia, Canada, and the United States of America impose sales taxes. The value-added tax is a general sales tax levied in France, Great Britain, and other European countries. It is applied to the increase in value of a product at each stage of manufacture and distribution.

Excise taxes are levied on the sales of specific products and privileges. They include taxes on sales of such items as petrol, tobacco and alcoholic beverages. Other excise taxes are the license tax, the franchise tax, and the severance tax. The license tax is levied on the right to participate in an activity such as selling alcoholic beverages, using a motor vehicle, getting married or going hunting or fishing. Franchise tax is a payment for the right to carry on a certain kind of business, such as operating a bus service or a public utility. Severance tax is levied on processing of natural resources, such as timber, natural gas, or petroleum.

Task 3. Answer the following questions.

1. What is taxation?
2. How does the government use taxes?
3. What are direct taxes levied on?
4. What are the most important kinds of taxes?
5. Why are property taxes called direct taxes?

6. What are income taxes levied on?
7. What are main types of income taxes?
8. What is capital gains tax?
9. In what cases losses are subtracted from overall profits?
10. What are the main types of taxes on transactions?
11. What do excise taxes include?

Task 4. Decide if the following statements are true or false

1. Property taxes are levied on sales of goods T/F
2. Capital gains tax is levied on profits received from the sale or exchange of real property T/F
3. General sales taxes is applied to the increase in value of a product at the first stage in its manufacture and distribution T/F
4. Property taxes ranks as the chief source of income for many local governments T/F
5. Income taxes are not considered as direct taxes T/F
6. Excise taxes are levied on the sales of specific products and privileges T/F
7. Income taxes are levied on imported goods T/F
8. Property taxes are levied on the value of houses or business equipment T/F
9. There are three types of income taxes T/F
10. Companies can not shift the cost of the tax to their customers by raising the price T/F
11. Excise tax is one of the types of taxes on transactions T/F

Task 5. Find Russian equivalents for the following kinds of taxes:

1.tax on a corporation	a.налог на оптовую торговлю
2.tax on capital	b.налог на доход от ценных бумаг
3.tax on income	c.налог на земельную собственность

4.tax on distributions	d.налог на корпорацию
5.tax on income from securities	e.подоходный налог
6.tax on land	f.налог на капитал
7.tax on tobacco	g.налог на доход
8.tax on profits	h.промысловый налог
9.tax on trade	i.налог на табак

ADDITIONAL TEXTS FOR READING

Origin

Until the 1930s most economic analysis did not separate out individual economics behavior from aggregate behavior. The dichotomy macroeconomy/microeconomy was first coined by the Norwegian Economist Ragnar Frisch in 1933 (Frisch 1933). With the Great Depression of the 1930s and the development of the concept of national income and product statistics, the field of macroeconomics began to expand. Particularly influential were the ideas of John Maynard Keynes, who formulated theories to try to explain the Great Depression. Before that time, comprehensive national accounts, as we know them today, did not exist.

One of the challenges of economics has been a struggle to reconcile macroeconomic and microeconomic models. Starting in the 1950s, macroeconomists developed micro-based models of macroeconomic behavior (such as the consumption function). Dutch economist Jan Tinbergen developed the first comprehensive national macroeconomic model, which he first built for the Netherlands and later applied to the United States and the United Kingdom after World War II. The first global macroeconomic model, Wharton Econometric Forecasting Associates LINK project, was initiated by Lawrence Klein and was mentioned in his citation for the Nobel Memorial Prize in Economics in 1980.

Theorists such as Robert Lucas Jr suggested (in the 1970s) that at least some traditional Keynesian (after British economist John Maynard Keynes) macroeconomic models were questionable as they were not derived from assumptions about individual behavior, although it was not clear whether the failures were in microeconomic assumptions or in macroeconomic models. However, New Keynesian macroeconomics has generally presented microeconomic models to shore up their macroeconomic theorizing, and some Keynesians have contested the idea that microeconomic foundations are essential, if the model is analytically useful. An analogy might be, that the fact that quantum physics is not fully consistent with relativity theory does not mean that relativity is false. Many important microeconomic assumptions have never been proved, and some have proved wrong.

The various schools of thought are not always in direct competition with one another, even though they sometimes reach differing conclusions. Macroeconomics is an ever evolving area of research. The goal of economic research is not to be "right," but rather to be accurate. It is likely that none of the current schools of economic thought perfectly capture the workings of the economy. They do, however, each contribute a small piece of the overall puzzle. As one learns more about each school of thought, it is possible to combine aspects of each in order to reach an informed synthesis.

Analytical approaches

The traditional distinction is between two different approaches to economics: Keynesian economics, focusing on demand; and supply-side (or neo-classical) economics, focusing on supply. Neither view is typically endorsed to the complete exclusion of the other, but most schools do tend clearly to emphasize one or the other as a theoretical foundation.

- Keynesian economics focuses on aggregate demand to explain levels of unemployment and the business cycle. That is, business cycle fluctuations should be reduced through fiscal policy (the government spends more or less depending on the situation) and monetary policy. Early Keynesian macroeconomics was "activist," calling for regular use of policy to stabilize the capitalist economy, while some Keynesians called for the use of incomes policies.

- Supply-side economics delineates quite clearly the roles of monetary policy and fiscal policy. The focus for monetary policy should be purely on the price of money as determined by the supply of money and the demand for money. It advocates a monetary policy that directly targets the value of money and does not target interest rates at all. Typically the value of money is measured by reference to gold or some other reference. The focus of fiscal policy is to raise revenue for worthy government investments with a clear recognition of the impact that taxation has on domestic trade. It places heavy emphasis on Say's law, which states that recessions do not occur because of failure in demand or lack of money.

Schools

- Monetarism, led by Milton Friedman, holds that inflation is always and everywhere a monetary phenomenon. It rejects fiscal policy because it leads to "crowding out" of the private sector. Further, it does not wish to combat inflation or deflation by means of active demand management as in Keynesian economics, but by means of monetary policy rules, such as keeping the rate of growth of the money supply constant over time.
- New Keynesian economics, which developed partly in response to new classical economics, strives to provide microeconomic foundations to Keynesian economics by showing how imperfect markets can justify demand management.
- Austrian economics is a laissez-faire school of macroeconomics. It focuses on the business cycle that arises from government or central-bank interference that leads to deviations from the rate of interest, and emphasizes the importance of credit and investment misallocation in business cycle fluctuations.
- Post-Keynesian economics represents a dissent from mainstream Keynesian economics, emphasizing the role of uncertainty, liquidity preference and the historical process in macroeconomics.
- New classical economics. The original theoretical impetus was the charge that Keynesian economics lacks microeconomic foundations -- i.e. its

assertions are not founded in basic economic theory. This school emerged during the 1970s. This school asserts that it does not make sense to claim that the economy at any time might be "out-of-equilibrium". Fluctuations in aggregate variables follow from the individuals in the society continuously re-optimizing as new information on the state of the world is revealed.

Market failure

In microeconomics, the term "market failure" does not mean that a given market has ceased functioning. Instead, a market failure is a situation in which a given market does not efficiently organize production or allocate goods and services to consumers. Economists normally apply the term to situations where the inefficiency is particularly dramatic, or when it is suggested that non-market institutions would provide a more desirable result. On the other hand, in a political context, stakeholders may use the term market failure to refer to situations where market forces do not serve the "public interest," a subjective assessment that is often made on social or moral grounds.

The four main types or causes of market failure are:

- Monopolies or other cases of abuse of market power where a "single buyer or seller can exert significant influence over prices or output"). Abuse of market power can be reduced by using antitrust regulations.
- Externalities, which occur in cases where the "market does not take into account the impact of an economic activity on outsiders." There are positive externalities and negative externalities. Positive externalities occur in cases such as when a television program on family health improves the public's health. Negative externalities occur in cases such as when a company's processes pollutes air or waterways. Negative externalities can be reduced by using government regulations, taxes, or subsidies, or by using property

rights to force companies and individuals to take the impacts of their economic activity into account.

- Public goods such as national defence and public health initiatives such as draining mosquito-breeding marshes. For example, if draining mosquito-breeding marshes was left to the private market, far fewer marshes would probably be drained. To provide a good supply of public goods, nations typically use taxes that compel all residents to pay for these public goods (due to scarce knowledge of the positive externalities to third parties/social welfare); and
- Cases where there is asymmetric information or uncertainty (information inefficiency). Information asymmetry occurs when one party to a transaction has more or better information than the other party. Typically it is the seller that knows more about the product than the buyer, but this is not always the case. Buyers in some markets have better information than the Sellers. For example, used-car salespeople may know how whether a used car has been used as a delivery vehicle or taxi, information that may not be available to buyers. An example of a situation where the buyer may have better information than the seller would be an estate sale of a house, as required by a last will and testament. A real estate broker purchasing this house may have more information about the house than the family members of the deceased.

This situation was first described by Kenneth J. Arrow in a seminal article on health care in 1963 entitled "Uncertainty and the Welfare Economics of Medical Care," in the American Economic Review. George Akerlof later used the term asymmetric information in his 1970 work The Market for Lemons. Akerlof noticed that, in such a market, the average value of the commodity tends to go down, even for those of perfectly good quality, because the buyer has no way of knowing whether the product they are buying will turn out to be a "lemon" (a defective product)

Macroeconomics

Macroeconomics is a branch of economics that deals with the performance, structure, and behavior of the economy as a whole (Snowden and Vane 2002). Macroeconomists study and seek to understand the determinants of aggregate trends in the economy with particular focus on national income, unemployment, inflation, investment, and international trade. In contrast, microeconomics is primarily focused on the determination of prices and the role of prices in allocating scarce resources.

While macroeconomics is a broad field of study, there are two areas of research that are emblematic of the discipline: The attempt to understand the causes and consequences of short-run fluctuations in national income (the business cycle), and the attempt to understand the determinants of long-run economic growth (increases in national income).

Macroeconomic models and their forecasts are used by both governments and large corporations to assist in the development and evaluation of economic policy and business strategy.

A **market economy** (also called a *free market economy* or a *free enterprise economy*) is an economic system in which the production and distribution of goods and services takes place through the mechanism of free markets guided by a free price system. In a market economy, businesses and consumers decide on their own volition what they will purchase and produce. Technically this means that the producer gets to decide what to produce, how much to produce, what to charge to customers for those goods, what to pay employees, etc., and not the government. These decisions in a free-market economy are influenced by the pressures of competition, supply, and demand. This is often contrasted with a planned economy, in which government decides what will be produced and in what quantities.

No pure market economy exists. Thus, almost all economies in the world today are mixed economies which combine varying degrees of market and command economy traits. For example, in the United States there are more market economy traits than in Western European countries.

A true free market economy is an economy in which all resources are owned by individuals, and in which decisions about the allocation of those resources are made by individuals without government intervention.

The United States has restrictions on the attainment of monopoly, but also grants monopoly rights in some cases. Less market restrictions are found in other countries, such as in Hong Kong and Singapore, according to the Index of Economic Freedom.

Free markets are also conflated with anarchy as many people believe that free market implies an absence of government. Only a few free market scholars advocate the elimination of government; most have believed government had a role to play, albeit a limited one (notably Adam Smith and Milton Friedman). Even anarcho-capitalists believe in the rule of law (either natural or contract) being defended by voluntarily-funded institutions.

Most free market scholars believe that governments should be limited to at least: operating a court system for the settlement of disputes, maintaining stable currency (combating inflation), protecting market competition and consumers, and protecting the country through national defense. These scholars debate and disagree with each other on whether or not governments are necessary to have government funded roads, schools, post offices, libraries, police stations, and fire stations, as some free market scholars believe the market can solve their externalities.

Although no country has ever had within its border an economy in which all markets were absolutely free, the term is typically not used in an absolute sense.

Many states which are said to have a capitalist system have a high level of market freedom, even if it is less than some would prefer.

Government Intervention

It is possible for a market economy to have government intervention in the economy. The key difference between market economies and planned economies lies not with the degree of government influence but whether that influence is used to coercively preclude private decision. In a market economy, if the government wants more steel, it collects taxes and then buys the steel at market prices. In a planned economy, a government which wants more steel simply orders it to be produced and sets the price by decree. An economy where both central planning and market mechanisms of production and distribution are present is known as a mixed economy. Germany's social market economy was one of the better functioning mixed economies, as microeconomists note that it had relatively free prices compared to other more socialist countries like the United Kingdom for much of the later 20th century.

The proper role for government in a market economy remains controversial. Most supporters of a market economy believe that government has a legitimate role in defining and enforcing the basic rules of the market. More controversial is the question of how strong a role the government should have in both guiding the economy and addressing the inequalities the market produces. For example, there is no universal agreement on issues such as protectionist tariffs, federal control of interest rates, and welfare programs.

Milton Friedman, along with many microeconomists, believes that too much government intervention and regulation can result in hampering or stopping the transmission of information necessary to allow the market to operate, what results, he believes, are very serious government externalities that can lead to inflation, deflation, recesions, and depressions. Milton Friedman believes that the

Great Depression was the result of a government created externalities and thus was responsible for the causes of the Great Depression.

Critisism of Market Economy

There are a variety of critics of the market as an organizing principle of an economy. These critics range from those who reject markets entirely, in favor of a planned economy, such as that advocated by some types of socialism, to those who merely wish to see them regulated to various degrees, and they range from those who believe that greed is inherently immoral to those who raise practical objections. One prominent practical objection is the claim that markets wreak havoc through their externalities (things that the market price does not take into account), for example through environmental pollution. Another is the claim that through the creation of monopolies, markets sow the seeds of their own destruction.

Some proponents of market economies believe that governments should not diminish market freedom because they disagree on what is a market externality and what are government created externalities, and disagree over what the appropriate level of intervention is necessary to solve market created externalities. Others believe that government should intervene to prevent market failure while preserving the general character of a market economy. In the model of a social market economy the state intervenes where the market does not meet political demands. John Rawls is a prominent proponent of this idea.

A Planned Economy

A **planned economy** (also known as **command economy** and **centrally planned economy**) is an economic system in which the state or government controls the factors of production and makes all decisions about their use and about the distribution of income. In such an economy, the planners decide what should be produced and direct enterprises to produce those goods. Planned economies are in contrast to unplanned economies, i.e. a market economy, where production, distribution, and pricing decisions are made by the private owners of the factors of production based upon their own interests rather than upon furthering some overarching macroeconomic plan.

A planned economy may either consist of state owned enterprises, private enterprises who are directed by the state, or a combination of both. Though "planned economy" and "command economy" are often used as synonyms, some make the distinction that under a command economy, the means of production are publicly owned. That is, a planned economy is "an economic system in which the government controls and regulates production, distribution, prices, etc." but a command economy, while also having this type of regulation, necessarily has substantial public ownership of industry. Therefore, command economies are planned economies, but not necessarily the reverse (example: Nazi Germany's private ownership yet use of the Four Year Plan could construe them as a planned economy, but not necessarily a command economy, while the Soviet Union with public ownership would be a command economy).

Important planned economies that existed in the past include the economy of the Soviet Union, which was for a time the world's second-largest economy. Beginning in the 1980s and 1990s, many governments presiding over planned economies began deregulating and moving toward market based economies by allowing the private sector to make the pricing, production, and distribution decisions. Although most economies today are market economies or mixed economies, planned economies exist in some countries such as Cuba and North Korea.

Support of Centrally Planned Economies

Supporters of planned economies cast them as a practical measure to ensure the production of necessary goods—one which does not rely on the vagaries of free markets.

- The government can harness land, labor, and capital to serve the economic objectives of the state (which, in turn, may be decided by the people through a democratic process). Consumer demand can be restrained in favor of greater capital investment for economic development in a desired pattern. The state can begin building a heavy industry at once in an underdeveloped economy without waiting years for capital to accumulate through the expansion of light industry, and without reliance on external financing.
- Consumers do not need money to express their economic demands; they may participate in democratic decision-making bodies (such as workers' councils or soviets) to voice their opinions and make decisions about the economy.
- A planned economy can maximize the continuous utilization of all available resources. This means that planned economies do not suffer from a business cycle. Under a planned economy, neither unemployment nor idle production facilities should exist beyond minimal levels, and the economy should develop in a stable manner, unimpeded by inflation or recession.
- A planned economy can serve social rather than individual needs: under such a system, rewards, whether wages or perquisites, are to be distributed according to the social value of the service performed. A planned economy eliminates the dependence of production on individual profit motives, which may not in themselves provide for all society's needs.
- While a market economy maximises wealth by evolution, a planned economy favors design. While evolution tends to lead to a local maximum in aggregate wealth, design is in theory capable of achieving a global maximum. For example, a planned city can be designed for efficient

transport, while organically grown cities tend to suffer from traffic congestion.

Taken as a whole, a centrally planned economy would attempt to substitute a number of firms with a single firm for an entire economy. As such, the stability of a planned economy has implications with the Theory of the firm. After all, most corporations are essentially 'centrally planned economies', aside from some token intra-corporate pricing (not to mention that the politics in some corporations resemble that of the Soviet Politburo). That is, corporations are essentially miniature centrally planned economies and seem to do just fine in a free market. As pointed out by Kenneth Arrow and others, the existence of firms in free markets shows that there is a need for firms in free markets; opponents of planned economies would simply argue that there is no need for a sole firm for the entire economy.

Objections to Central Planning

Critics of planned economies argue that planners cannot detect consumer preferences, shortages, and surpluses with sufficient accuracy and therefore cannot efficiently co-ordinate production (in a market economy, a free price system is intended to serve this purpose). For example, during certain periods in the history of the Soviet Union, shortages were so common that one could wait hours in a queue to buy basic consumer products such as shoes or bread. These shortages were due in part to the central planners deciding, for example, that making tractors was more important than making shoes at that time, or because the commands were not given to supply the shoe factory with the right amount of leather, or because the central planners had not given the shoe factories the incentive to produce the required quantity of shoes of the required quality. This difficulty was first noted by economist Ludwig von Mises, who called it the "economic calculation problem". Economist János Kornai developed this into a shortage economy theory (advocates could claim that shortages were not primarily caused by lack of supply). There is also the problem of surpluses. Surpluses indicate a waste of labor and materials that could have been applied to more pressing needs of society. Critics of central planning say that a market economy prevents long-term surpluses because the operation of supply and demand causes the price to sink when supply begins exceeding demand, indicating to producers to stop production or face profit losses. This frees resources to be applied to satisfy short-term shortages of other commodities, as determined by their rising prices as demand begins exceeding supply. It is argued that this "invisible hand" prevents long-term shortages and surpluses and allows maximum efficiency in satisfying the wants of consumers. Critics argue that since in a planned economy prices are not allowed to float freely, there is no accurate mechanism for determine what is being produced in unnecessarily large amounts and what is being produced in insufficient amounts. They argue that efficiency is best achieved through a market economy where individual producers each make their own production decisions based on their own profit motive.

Another criticism of central planning is that it is less likely to promote innovation than a free market economy. In the latter, inventors can reap huge benefits by patenting new technology, so there is arguably much more incentive to innovate. Additionally, the top down structure of a centrally planned economy dictates a hegemonic operating culture - whereas in a free market economy several models of operating can compete simultaneously in a manner similar to organisms in an ecosystem.

Some who oppose comprehensive planned economies argue that some central planning is justified. In particular, it is possible to create unprofitable but socially useful goods within the context of a market economy. For example, one could produce a new drug by having the government collect taxes and then spend the money for the social good. On the other hand, opponents of such central planning say that "absent the data about priorities conveyed through price signals created by freely acting individuals, [it is questionable] whether determinations about what is socially important can even be made at all." Opponents do not dispute that something useful can be produced if money is expropriated from private businesses and individuals, but their complaint is that "it’s far from certain that those monies could not have been spent better" if individuals were allowed to spend and invest as they wished according to their own wants. We can see things of value being produced by the state taxing and using those funds to undertake projects which are believed to be social goods, but we cannot see what social goods have *not* been produced due to wealth taken out of the hands of those who would have invested and spent their money in other ways according to their own goals. These opponents of central planning argue that the only way to determine what society actually wants is by allowing private enterprise to use their resources in competing to meet the needs of consumers, rather those taking resources away and allowing government to direct investment without responding to market signals. According to Tibor R. Machan, "Without a market in which allocations can be made in obedience to the law of supply and demand, it is difficult or impossible to funnel resources with respect to actual human preferences and goals."

Critics also hold that certain types of command economies may require a state which intervenes highly in people's personal lives. For example, if the state directs all employment then one's career options may be more limited. If goods are allocated by the state rather than by a market economy, citizens cannot, for example, move to another location without state permission because they would not be able to acquire food or housing in the new location, as the necessary resources were not preplanned (however, advocates of planned economies may point out that a market economy does not guarantee the existence of food and housing at the new location, either).

Transition from a Planned To a Market Economy

The shift from a command economy to a market economy has proven to be difficult; in particular, there were no theoretical guides for doing so before the 1990s. One transition from a command economy to a market economy that is widely considered to be successful is that of the People's Republic of China, in which there was a period of some years lasting roughly until the early 1990s during which both the command economy and the market economy coexisted, so that nobody would be much worse off under a mixed economy than a command economy, while some people would be much better off. Gradually, the parts of the economy under the command economy decreased until the mid-1990s when resource allocation was almost completely determined by market mechanisms.

By contrast, the Soviet Union's transition was much more problematic and its successor republics faced a sharp decline in GDP during the early 1990s. While the transition to a market economy proved difficult, many of the post-Soviet states have been experiencing strong, resource-based economic growth in recent years, though the levels vary substantially. However a majority of the former Soviet Republics have not yet reached pre-collapse levels of economic development.

Free trade and movement of factors of production

Free trade laissez faire theory argues that economic efficiency is achieved in cases where free movement (laissez passer) of the "factors of production" is permitted. Karl Polanyi in "The Great Transformation", however, argued that historically whenever laissez faire policies are adopted, legal moves to prevent the free movement of one of the factors of production always occur (for example current neo-liberal attempts to free the movement of capital and resources are today increasingly tied to immigration controls).

Human capital and intellectual capital

Contemporary analysis distinguishes capital goods from other forms of capital such as human capital. Human capital is acquired through education and training, whether formal or on-the-job. A more recent coinage is intellectual capital, used especially as to information technology.

Prior to the Information Age the land, labor, and capital were used to create substantial wealth due to their scarcity. During the Information Age (circa 1971-1991), the Knowledge Age (circa 1991 to 2002), and the Intangible Economy (2002-present) the primary factors of production have become less concrete. These factors of production are knowledge, collaboration, process-engagement, and time quality. According to economic theory, a "factor of production" is used to create value and economic performance. As the four modern-day factors are all essentially abstract, the current economic age has been called the Intangible Economy. Intangible factors of production are subject to network effects and the contrary economic laws such as the law of increasing returns. It is therefore important to differentiate between conventional (tangible) economics and intangible economics when discussing issues related to factors of production which change according to the economic era that society is experiencing. For example, *land* was a key factor of production in the Agricultural Age.

Combination of factors

Some economists mention enterprise, entrepreneurship, individual capital or just "leadership" as a *fourth* factor. However, this seems to be a form of labor or "human capital." When differentiated, the payment for this factor of production is called profit. This is when entrepreneurs think of ideas, organize the other three factors of production, and take risks with their own money and the financial capital of others.

In a market economy, entrepreneurs combine the factors of production, land, labor, and capital in an innovative way to make a profit. In a planned economy, central planners decide how land, labor, and capital should be used to provide for maximum benefit for all citizens.

Income Elasticity of Demand

Studying the theory of demand we can assume that there is relationship between price, income and quantity, but this assumption itself can not allow us to see how much the quantity demanded is affected by a price change for a good or an income change. The relationship varies from one good to another.

One of the most important of these relationships is income elasticity of demand. The income elasticity of demand is how much the quantity demanded depends on changes in income if other factors are constant. The income elasticity is the percentage change in quantity following one-percent change in income if other factors are constant.

The coefficient is mainly positive as with the income increased a consumer buys more of the most products, and when the income decreases, the quantity demanded falls.

The income elasticity for food in the United States is about 0.2. A few goods such as dry beans have negative income elasticities. If elasticity is above zero, the product is an inferior good.

Price Elasticity of Demand and Supply

There is relationship between demand and price. How much demand for commodity is affected by a change in price is called elasticity of demand. If a small change of price results in a large change in demand, the demand is called elastic, if the demand changes only a little, it is called inelastic. The price elasticity of demand coefficient is negative as demand usually falls with a rise in price.

The price elasticity of supply shows the percentage change in the quantity supplied resulting from a one-percent change in price.

As an increase in the quantity supplied is normally a result of a rise in price, the coefficient is usually positive. We have a “0” (zero) elasticity when a price change results in no quantity supplied change. This is called a perfectly inelastic supply. Provided the elasticities vary between zero and one, the supply is called inelastic. With coefficients greater than one, the supply is called elastic. The percentage change in quantity is greater than the corresponding percentage change in price.

Agricultural supply is mostly inelastic because of the high proportion of such inputs as land, buildings, and machinery. The elasticities of agricultural commodities (potatoes, wheat, fruits, eggs, milk) vary greatly. Because of increasing specialization of production, of farm animal products, in particular, elasticities for such commodities as pigs and broilers have decreased in recent years.

Purposes and effects of taxation

Funds provided by taxation have been used by states and their functional equivalents throughout history to carry out many functions. Some of these include expenditures on war, the enforcement of law and public order, protection of property, economic infrastructure (roads, legal tender, enforcement of contracts, etc.), public works, social engineering, and the operation of government itself. Most modern governments also use taxes to fund welfare and public services. These services can include education systems, health care systems, pensions for the elderly, unemployment benefits, and public transportation. Energy, water and waste management systems are also common public utilities. Colonial and moderning states have also used cash taxes to draw or force reluctant subsistence producers into cash economies.

Governments use different kinds of taxes and vary the tax rates. This is done to distribute the tax burden among individuals or classes of the population involved in taxable activities, such as business, or to redistribute resources between individuals or classes in the population. Historically, the nobility were supported by taxes on the poor; modern social security systems are intended to support the poor, the disabled, or the retired by taxes on those who are still working. In addition, taxes are applied to fund foreign and military aid, to influence the macroeconomic performance of the economy (the government's strategy for doing this is called its fiscal policy - see also tax exemption), or to modify patterns of consumption or employment within an economy, by making some classes of transaction more or less attractive.

The resource collected from the public through taxation is always greater than the amount which can be used by the government. The difference is called *compliance cost*, and includes for example the labour cost and other expenses incurred in complying with tax laws and rules. The collection of a tax in order to spend it on a specified purpose, for example collecting a tax on alcohol to pay directly for alcoholism rehabilitation centres, is called hypothecation. This practice is often disliked by finance ministers, since it reduces their freedom of action. Some economic theorists consider the concept to be intellectually dishonest since (in reality) money is fungible. Furthermore, it often happens that taxes or excises initially levied to fund some specific government programs are then later diverted to the government general fund. In some cases, such taxes are collected in fundamentally inefficient ways, for example highway tolls.

Some economists, especially neo-classical economists, argue that all taxation creates market distortion and results in economic inefficiency. They have therefore sought to identify the kind of tax system that would minimize this distortion. Also, one of every government's most fundamental duties is to administer possession and use of land in the geographic area over which it is sovereign, and it is considered economically efficient for government to recover for public purposes the additional value it creates by providing this unique service.

Since governments also resolve commercial disputes, especially in countries with common law, similar arguments are sometimes used to justify a sales tax or value added tax. Others (e.g. libertarians) argue that most or all forms of taxes are immoral due to their involuntary (and therefore eventually coercive/violent) nature. The most extreme anti-tax view is anarcho-capitalism, in which the provision of *all* social services should be a matter of voluntary private contracts.

INFLATION

In mainstream economics, the word "**inflation**" refers to a general rise in prices measured against a standard level of purchasing power. Previously the term was used to refer to an increase in the money supply, which is now referred to as expansionary monetary policy or monetary inflation. Inflation is measured by comparing two sets of goods at two points in time, and computing the increase in cost not reflected by an increase in quality. There are, therefore, many measures of inflation depending on the specific circumstances. The most well known are the CPI which measures consumer prices, and the GDP deflator, which measures inflation in the whole of the domestic economy.

The prevailing view in mainstream economics is that inflation is caused by the interaction of the supply of money with output and interest rates. Mainstream economist views can be broadly divided into two camps: the "monetarists" who believe that monetary effects dominate all others in setting the rate of inflation, and the "Keynesians" who believe that the interaction of money, interest and output dominate over other effects. Other theories, such as those of the Austrian school of economics, believe that an inflation of overall prices is a result from an increase in the supply of money by central banking authorities.

Related terms include: deflation, a general falling level of prices; disinflation, the reduction of the rate of inflation; hyper-inflation, an out-of-control inflationary spiral; stagflation, a combination of inflation and poor economic growth; and reflation, which is an attempt to raise prices to counteract deflationary pressures.

THE ROLE OF INFLATION IN THE ECONOMY

In the long run, inflation is generally believed to be a monetary phenomenon, while in the short and medium term, it is influenced by the relative elasticity of wages, prices and interest rates. [1] The question of whether the short-term effects last long enough to be important is the central topic of debate between monetarist and Keynesian schools. In monetarism, prices and wages adjust quickly enough to make other ass factors merely marginal behavior on a general trendline. In the Keynesian view, prices and wages adjust at different rates, and these differences have enough effects on real output to be "long term" in the view of people in an economy.

A great deal of economic literature concerns the question of what causes inflation and what effect it has. A small amount of inflation is often viewed as having a positive effect on the economy. One reason for this is that it is difficult to renegotiate some prices, and particularly wages, downwards, so that with generally increasing prices it is easier for relative prices to adjust. Many prices are "sticky downward" and tend to creep upward, so that efforts to attain a zero inflation rate (a constant price level) punish other sectors with falling prices, profits, and employment. Efforts to attain complete price stability can also lead to deflation, which is generally viewed as a negative outcome because of the significant downward adjustments in wages and output that are associated with it.

Inflation is also viewed as a hidden risk pressure that provides an incentive for those with savings to invest them, rather than have the purchasing power of those savings erode through inflation. In investing inflation risks often cause investors to take on more systematic risk, in order to gain returns that will stay ahead of expected inflation. Inflation is also used as an index for cost of living adjustments and as a peg for some bonds. In effect, inflation is the rate at which previous economic transactions are discounted economically.

Inflation also gives central banks room to maneuver, since their primary tool for controlling the money supply and velocity of money is by setting the lowest interest rate in an economy - the discount rate at which banks can borrow from the central bank. Since borrowing at negative interest is generally ineffective, a positive inflation rate gives central bankers "ammunition", as it is sometimes called, to stimulate the economy.

However, in general, inflation rates above the nominal amounts required to give monetary freedom, and investing incentive, are regarded as negative, particularly because in current economic theory, inflation begets further inflationary expectations.

- Increasing *uncertainty* may discourage investment and saving.
- *Redistribution*
  - It will redistribute income from those on fixed incomes, such as pensioners, and shifts it to those who draw a variable income, for example from wages and profits which may keep pace with inflation.
  - Similarly it will redistribute wealth from those who lend a fixed amount of money to those who borrow. For example, where the government is a net debtor, as is usually the case, it will reduce this debt redistributing money towards the government. Thus inflation is sometimes viewed as similar to a hidden tax.
- *International trade*: If the rate of inflation is higher than that abroad, a fixed exchange rate will be undermined through a weakening balance of trade.
- *Shoe leather costs*: Because the value of cash is eroded by inflation, people will tend to hold less cash during times of inflation. This imposes real costs, for example in more frequent trips to the bank. (The term is a humorous

reference to the cost of replacing shoe leather worn out when walking to the bank.)

- *Menu costs*: Firms must change their prices more frequently, which imposes costs, for example with restaurants having to reprint menus.
- *Relative Price Distortions*: Firms do not generally synchronize adjustment in prices. If there is higher inflation, firms that do not adjust their prices will have much lower prices relative to firms that do adjust them. This will distort economic decisions, since relative prices will not be reflecting relative scarcity of different goods.
- *Hyperinflation*: if inflation gets totally out of control (in the upward direction), it can grossly interfere with the normal workings of the economy, hurting its ability to supply.
- *Inflation tax* when a government can improve its net financial position by allowing inflation, then this represents a tax on certain holders of currency. Governments may decide to use this "stealth tax" in order to avoid hard fiscal decisions to cut expenditures, raise taxes, or confront government unions with greater efficiency.
- *Bracket Creep* is related to the inflation tax. By allowing inflation to move upwards, certain sticky aspects of the tax code are met by more and more people. Commonly income tax brackets, where the next dollar of income is taxed at a higher rate than previous dollars. Governments that allow inflation to "bump" people over these thresholds are, in effect, allowing a tax increase because the same real purchasing power is being taxed at a higher rate.

As noted, some economists see moderate inflation as a benefit; some business executives see mild inflation as "greasing the wheels of commerce." A very few economists have advocated reducing inflation to zero as a monetary policy goal - particularly in the late 1990s at the end of a long disinflationary period, when the policy seemed within reach.

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